

**Before The
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554**

In the Matter of)	
)	
Federal-State Joint Board on)	
Universal Service)	CC Docket No. 96-45
)	
1998 Biennial Regulatory Review -)	
Streamlined Contributor Reporting)	
Requirements Associated with)	
Administration of Telecommunications)	CC Docket No. 98-171
Relay Service, North American Numbering)	
Plan, Local Number Portability, and)	
Universal Service Support Mechanisms.)	
)	
Telecommunications Services for)	
Individuals with Hearing and Speech)	
Disabilities, and the Americans with)	CC Docket No. 90-571
Disabilities Act of 1990.)	
)	
Administration of the North American)	
Number Plan and North American)	CC Docket No. 92-237
Numbering Plan Cost Recovery)	NSD File No. L-00-72
Contribution Factor and Fund Size.)	
)	
Number Resource Optimization)	CC Docket No. 99-200
)	
Telephone Number Portability)	CC Docket No. 95-116
)	
Truth-in-Billing and Billing Format)	CC Docket No. 98-170

**SUPPLEMENTAL COMMENTS OF THE
NATIONAL ASSOCIATION OF STATE UTILITY CONSUMER
ADVOCATES**

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Executive Summary

The National Association of State Utility Consumer Advocates (“NASUCA”),¹ presents these supplemental comments on the federal universal service contribution mechanism, in response to the Second Further Notice of Proposed Rulemaking.² NASUCA demonstrates that major structural changes to the contribution mechanism are still not necessary. This makes the three specific mechanisms on which the Federal Communications Commission (“Commission”) seeks comment fundamentally unnecessary. Each of the three proposed mechanisms also violates the fundamental requirement of the law that federal universal service contributions come from providers of interstate services. Each of the three proposed mechanisms also imposes unnecessary costs on the public switched telephone network.

A connection-based mechanism or a numbers-based mechanism, such as proposed by those who would benefit from such a change, conflicts with the statutory provisions for the federal universal service support mechanism.³ A connection-based mechanism

¹ NASUCA is an association of 42 consumer advocates in 40 states and the District of Columbia. NASUCA’s members are designated by the laws of their respective states to represent the interests of utility consumers before state and federal regulators and in the courts. See, e.g., Chapter 4911, Ohio Rev. Code.

² Report and Order and Second Further Notice of Proposed Rulemaking, FCC 02-239 (rel. 13, 2002). The Report and Order on the universal service fund contribution mechanism will be referred to here as the “USF Contrib Mech R&O”; the Second Further Notice of Proposed Rulemaking will be referred to as the “SFNPRM.” NASUCA previously filed comments in Response to the Further Notice of Proposed Rulemaking (rel.) (“FNPRM”), and in response to the Notice of Proposed Rulemaking (“NPRM”) (rel.).

³ The numbers-based mechanism was introduced by AT&T in an October 2, 2002 *ex parte*. The numbers-based mechanism is actually a variant of the connection-based mechanism, as the Commission admits. SFNPRM, ¶ 96. Given this, except when referring specifically to the numbers-based mechanism (see Section E.3 below), these comments will refer to all three Commission proposals as connection-based mechanisms.

inequitably places the same burden of contribution on those who do not use the interstate network as on those who are heavy users of the network.⁴

A. Introduction

In the FNPRM released February 26, 2002, the Commission asserted that trends in the telecommunications marketplace could erode the contribution base for the Commission-ordered universal service fund (“USF”). FNPRM, ¶ 1. As part of its proceeding to revisit the contribution mechanism, the Commission requested comments on:

- Whether to assess contributions based on the number and capacity of connections provided to the public network. *Id.*, ¶ 2.
- Whether a connection-based assessment would ensure the long-term stability and efficiency of the contribution system in a dynamic telecommunications marketplace. *Id.*
- Other reforms to the contribution process. *Id.*

NASUCA was among many parties commenting in response to the FNPRM. NASUCA’s comments questioned whether the interstate revenues on which USF contributions should be assessed were in fact “eroding.” NASUCA also showed that the connection-based contribution mechanism discussed in the FNPRM violated the statutory requirement that **all** interstate carriers contribute to universal service in an equitable manner. See 47 U.S.C. § 254(d).

⁴ The Commission previously rejected a per-line approach to assessments because “the need to establish line equivalency ratios would make such an approach difficult to administer....” FNPRM, ¶ 44. Now, the Commission is proposing to base the per-connection approach on the “maximum capacity of the connection.” This is equally arbitrary.

In the USF Contrib Mech R&O, the Commission has done much to reform the current revenue-based contribution mechanism, including prohibiting carriers from marking up USF line items on customers' bills.⁵ The Commission also attempted to plug a hole in the contribution mechanism by raising the wireless safe harbor from 15% to 28.5%.⁶

Despite these improvements, the Commission is still focused on the perceived need to make major structural changes in the mechanism by which USF contributions are assessed. Despite considerable opposition from carriers, regulators and consumers, the Commission remains focused on adopting a connection-based mechanism.⁷

The adoption of a connection-based mechanism would represent a substantial, unnecessary and unreasonable change in the way in which USF contributions are collected. It would be far better -- and far easier -- to continue the reform of the revenue-

⁵ USF Contrib Mech R&O, ¶ 45. NASUCA had argued that the Commission should forbid carriers from placing USF line items on customers' bills. Initial Comments (June 25, 2001) at 7-17. The Commission's ruling is at least preferable to the carriers' proposal that they be allowed to include company-determined markups on the USF line items. USF Contrib Mech R&O, ¶ 43, n. 120.

⁶ USF Contrib Mech R&O, ¶ 21. The wireless safe harbor allows cellular, PCS and certain SMR providers to assume that the set percentage (now 28.5%) of their revenues are interstate. If the carrier has a lower percentage of interstate revenues, the carrier can report less than the safe harbor amount, but must be prepared to demonstrate the appropriate number to the Commission or the Administrator of the USF. See *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Memorandum Opinion and Order and Further Notice Of Proposed Rulemaking, 13 FCC Rcd 21252, ¶ 11. Carriers with a higher percentage can take advantage of the safe harbor amount.

⁷ Again in this context, NASUCA would note agreement with Consumers Union *et al.* that the Commission's systematic disregard of earlier comments supporting the revenue-based mechanism and attacking the connection-based mechanism, and acceptance of an *ex parte* as the basis for its own proposal, violates "[b]asic principles of due process and administrative law...." Consumers Union, *et al.* Comments (April 22, 2002) at 4. That error is exacerbated by the lack of independent support for the Commission's proposal.

based mechanism, which assesses providers based on usage of -- rather than on customers' access to -- interstate services.⁸

The Commission should, at the very least, wait to assess the impacts of the changes in the revenue-based mechanism resulting from the USF Contrib Mech R&O, before moving ahead with substantial structural changes to the USF contribution mechanism. Examining additional ways to more accurately assess interstate telecommunications traffic would be another way to improve the efficiency of the federal universal service support mechanism. The Commission must also take aggressive steps to ensure that the size of the federal USF stays within reasonable bounds, as discussed in Section D below.

The Commission asked for comment on a connection-based mechanism in the May 8, 2001 NPRM (at ¶ 25), among a long list of other items. The FNPRM gave no indication why the Commission had seized on the single alternative of a connection-based mechanism -- and one which had specific rates attached to it -- compared to all the other solutions provided by commenters. FNPRM, ¶ 29. Equally, the SFNPRM addresses the support for a connection-based mechanism -- and proposes three specific structures for connection-based mechanisms -- but virtually ignores the many parties who opposed such a mechanism.

The Commission states, "An analysis of the record reveals interest in a connection-based methodology..." (SFNPRM, ¶ 4), and asserts that "many parties agree

⁸ Although Section 254(d) requires "[e]very telecommunications carrier that provides interstate telecommunications services" to contribute to universal service, Commission policy up until now has allowed this obligation to be passed on to customers. NASUCA has opposed this misapplication of the law in the past and continues to do so in this proceeding.

that a connection-based contribution methodology will best ensure the long-term viability of the Commission's universal service mechanisms....” *Id.*, ¶5. This ignores the comments of many parties, including NASUCA, who were opposed to the adoption of a connection-based mechanism. This neglect of the other side of the argument is especially troubling, given how substantial is the proposed change, the lack of factual basis for the change, and the legal problems of a connection-based mechanism. Fundamentally, these flaws are fatal to all three specific mechanisms proposed by the Commission.

B. The forces driving changes in the federal mechanism

In the opening paragraphs of the SFNPRM, the Commission now identifies two themes that supposedly threaten “the long-term viability of any revenue-based system.”⁹ The first is that “interstate telecommunications revenues are becoming increasingly difficult to identify as customers migrate to bundled packages of interstate and intrastate telecommunications and non-telecommunications products and services.”¹⁰ The second theme is that “[i]ncreased competition is also placing downward pressure on interstate rates and revenues, which also contributes to the decline in the contribution base.”¹¹

With regard to the Commission's first theme, it does not appear that the record here presents concrete examples of the supposed difficulty of assessing the interstate

⁹ *Id.*

¹⁰ *Id.*

¹¹ *Id.* These themes are little different from those set forth in the February 2002 FNPRM, where the Commission noted three causes for the supposed decline in the contribution base: 1) “migration to new products and services”; 2) “local exchange carrier entry into the long distance market” and 3) “related price competition.” FNPRM, ¶ 7.

portion of bundled inter- and intrastate services. Real-life examples are vital to justify a major change like the move to a connection-based mechanism.

It may be true that “market-place developments have blurred the distinctions between interstate/intrastate and telecommunications/non-telecommunications revenues.” FNPRM, ¶ 12. This “blurring,” however, cannot obscure the legal reality that the FCC’s assessment for the interstate USF can be assessed only on providers of interstate services. 47 U.S.C. § 254(d); *Texas Office of Public Utility Counsel v. FCC* (“*TOPUC I*”), 183 F.3d 393, 448 (5th Cir. 1999).

In any event, this “blurring” of distinctions is scarcely an insurmountable problem. The Commission addressed the same problem with identifying the interstate portion of the joint and common costs of the network, in order to allocate costs between the inter- and intrastate jurisdictions.¹² There, the Commission decided that 25% of the joint and common costs of the network would be allocated to the interstate jurisdiction.¹³ This decision has underlain many of the Commission’s policies since that time. Thus the Commission could also reasonably determine that at least 25% of the revenues from a bundle of interstate and intrastate services should be allocated to the USF contribution

¹² See, e.g., *In the Matter of Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 80-286, 96 F.C.C.2d 781; 1984 FCC LEXIS 2905; 55 Rad. Reg. 2d (P & F) 659.

¹³ *Id.*, ¶ 12.

base.¹⁴ The Commission could establish a “safe harbor” similar to that used by wireless carriers, for these bundles.¹⁵

In a Petition for Reconsideration or Clarification of the USF Contrib Mech R&O filed January 29, 2003, Nextel Communications Inc. notes (at 6) that “some carriers have developed the capability to conduct aggregated studies of their traffic flows to determine a reasonable proxy of the proportion of interstate traffic, which in turn provides a reasonable proxy of a carrier’s proportion of interstate revenue.” It is not clear why more -- if not all -- carriers would not be able to develop such proxies. Thus the issue is not that interstate revenues in bundles cannot be identified; the issue is how to identify them.

As to the Commission’s second theme, the reduced rates that are the product of increased competition in the interstate market¹⁶ will have a substantial impact only if the reduction outstrips the increase in traffic that economic theory would expect from the reduced prices. Further, the fact that consumers are migrating to “mobile wireless and Internet-based services”¹⁷ means that those services should more closely be scrutinized as a source of contribution to the interstate USF.¹⁸

¹⁴ Indeed, just as the Commission has assumed total interstate jurisdiction over advanced services that combine intra- and interstate components, in this context the Commission could also assert interstate USF jurisdiction over bundles that mix inter- and intrastate services. In that case, 100% of the bundle revenue could be assessed for a USF contribution.

¹⁵ As discussed in Section D, below, the Commission could also establish three zones for revenues in this context.

¹⁶ USF Contrib Mech R&O, ¶ 3.

¹⁷ *Id.*

¹⁸ The Commission previously discussed “voice over Internet protocol” (“VoIP”) as a threat to the “overall amount of assessable revenues reported under the current system.” FNPRM, ¶ 13. The threat, which the General Accounting Office described as “not immediate ... but ... long-term” (*id.*, n. 32) actually depends on the Commission’s decisions on how to classify such traffic, whether as a telecommunications service or an information service. VoIP is not mentioned in the SFNPRM.

It should be clear that none of these problems are sufficient to justify a major restructuring of the USF contribution mechanism. There is little support in the record for such a change. The lack of such support calls into question the entire rationale for a connection-based mechanism.

C. The current status of the fund and the need for change

The Commission states, “[W]e seek to further refine the record in this proceeding.” SFNPRM, ¶ 66. NASUCA’s April 22, 2002 Initial Comments compiled statistics that showed that there was no need for significant structural change in the USF contribution mechanism. Those statistics -- updated as much as possible -- are repeated here.

Table 1 shows that, from the first quarter of 1999 to the first quarter of 2003, or four years, the contribution base actually used to calculate the USF contribution factor showed fluctuations, but these fluctuations do not reflect any statistically significant decrease or increase. Chart 1 which follows the Table graphically displays the contribution base and USF fund size since 1999.

Table 1

	Contribution base (a) (in billions)	Total USF Need (b) (in billions)	Contribution Factor (c)
1 st quarter 2003	17.23	1.50	0.087094 (d)
4 th quarter 2002	16.98	1.59	0.093397 (d)
3 rd quarter 2002	17.16	1.51	0.087735 (d)
2 nd quarter 2002	19.03	1.39	0.072805
1 st quarter 2002	20.25	1.38	0.068086
4 th quarter 2001	19.40	1.34	0.069187
3 rd quarter 2001	19.94	1.37	0.068941
2 nd quarter 2001	20.30	1.40	0.068823
1 st quarter 2001	20.26	1.35	0.066827
4 th quarter 2000	20.96	1.19	0.056688
3 rd quarter 2000	20.20	1.12	0.055360
2 nd quarter 2000	19.38	1.11	0.057101
1 st quarter 2000	18.96	1.11	0.058770
4 th quarter 1999	18.91	1.10	0.058170
3 rd quarter 1999	18.99	1.10	0.057925
2 nd quarter 1999	18.31	0.84	0.045876
1 st quarter 1999	18.35	0.91	0.04959
NOTES: (a) Quarterly Contribution Base (after 1% uncollectibles are removed) (b) Total Program Collection (c) cost/revenues (d) These are the calculated contribution factors. In a decision released June 13, 2002, the Commission stabilized the contribution factor for 3Q02-1Q03 at 0.072805 by using unused funds from the schools and libraries support mechanism. ¹⁹ Source: Contribution Factor Public Notices.			

¹⁹ See *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, First Report and Order (rel. June 13, 2002).

Chart 1

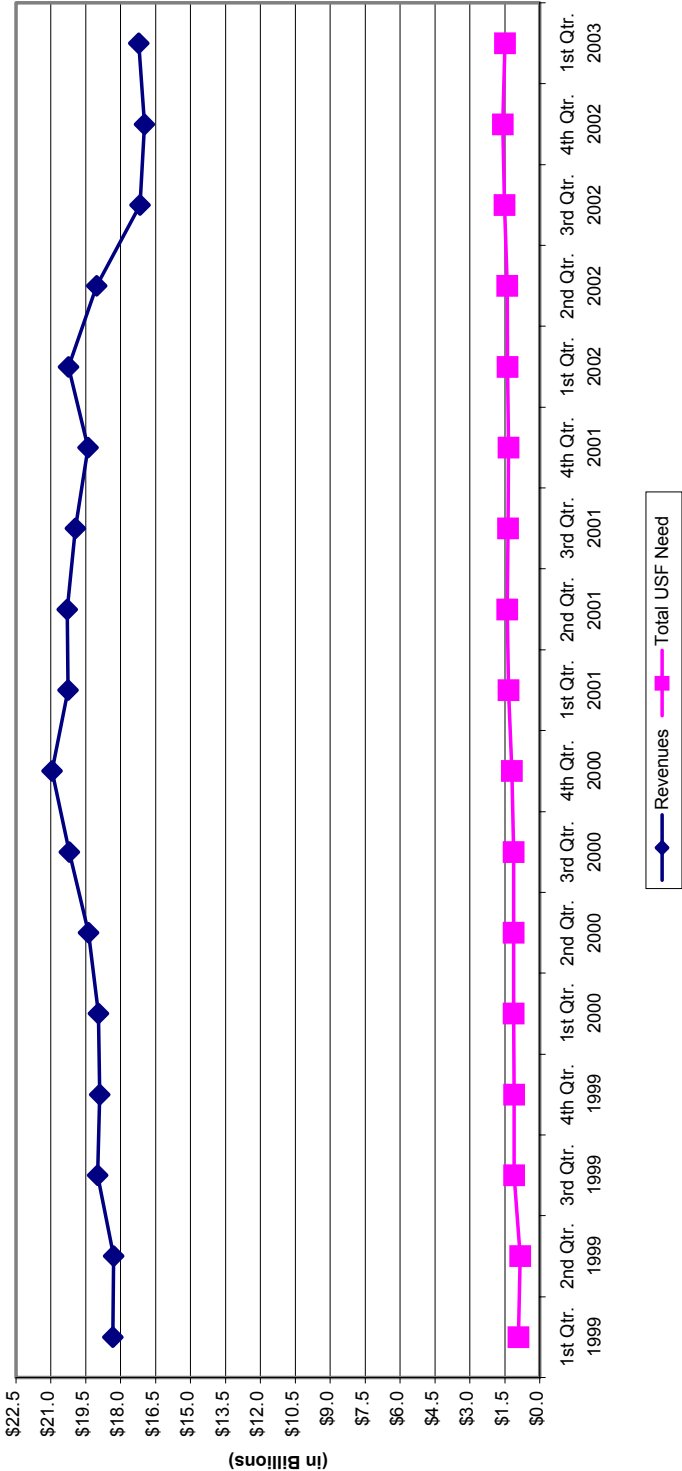
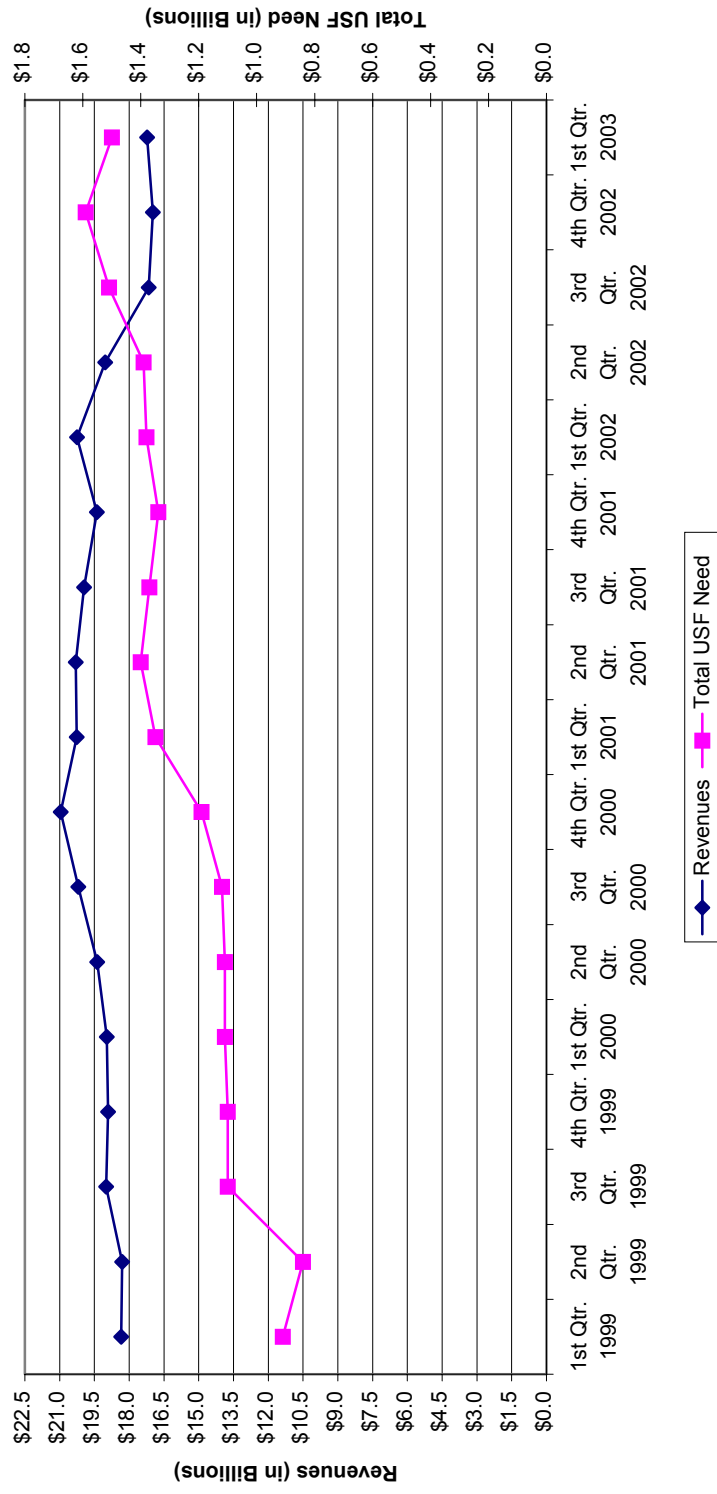


Chart 2

Chart 2 on the following page provides a different perspective and clearly shows the source of the problem in the USF contribution mechanism, that being the size of and increases in the USF itself:

Chart 2



The problem is not the growth or lack of growth in the contribution base. Indeed, when reviewed on an annual basis, there has been no significant downward trend in the contribution base:

Table 2

Year	Contribution base (in \$ billions)	Total USF need(in \$ billions)
2002	73.3	5.87
2001	79.9	5.46
2000	79.5	4.53
1999	74.6	3.95

During this period the assessed contribution base has declined by less than 2%, but the USF need has grown by almost 1½ times. It is clear that the growth in the fund -- not the decline in the contribution base -- is driving the increase to the contribution factor.

In the FNPRM, the Commission stated that it is seeking stability in the universal service mechanism. FNPRM, ¶ 17. This sentiment is repeated in the SFNPRM. SFNPRM, ¶ 3. It should be clear that no mechanism can provide stability unless there is stability in the size of the USF. The size of the fund is a matter that is within the control of the Commission.

The original proponents of the connection-based mechanism, the now-dissolved CoSUS, declared that the USF was in a so-called “death spiral,” where the revenue base on which USF contributions are assessed shrinks, and the amount of contributions needed expands, so that the assessment factor grows and grows. CoSUS Comments (April 22, 2002) at 24. Notably, the Commission does not mention the “death spiral” prophecy. Perhaps that is because the record shows that the patient is nowhere near critical

condition. As shown here, the supposedly “shrinking revenue base” can be addressed without adopting a connection-based mechanism.

Absent a verifiable downward trend in the overall interstate revenue base on which the USF is assessed, the Commission is incorrect in its estimation that there are problems with the current revenue-based mechanism sufficient to require significant restructuring. One correct tack to maintain the USF is to ensure that all sources of interstate traffic are assessed. Thus if less contribution is coming from IXC's, more contribution should be coming from the RBOCs, wireless and other providers of interstate telecommunications services. Equally importantly, the Commission must ensure that the size of the fund itself is kept within reasonable limits.

D. Suggestions for addressing problems without major structural changes

The current USF consists of five parts: the high-cost fund for non-rural carriers (47 C.F.R. § 54.309 et seq.; § 54.901 et seq.); the high-cost fund for rural carriers (47 C.F.R. § 54.301 et seq.); the low-income fund (47 C.F.R. § 54.400 et seq.); the advanced services fund for schools and libraries (47 C.F.R. § 54.500 et seq.); and the advanced services fund for rural health care. 47 C.F.R. §54.601 et seq.

The following table shows the relative size of the five parts for the first quarter of 2003.²⁰

²⁰ *Federal Universal Service Support Mechanisms Fund Size Projections for the First Quarter 2003*, Universal Service Administrative Company (Nov. 1, 2002).

TABLE 3

	\$M	\$ Annualized	% of total
Non-rural high cost	221.0	884.0	14.3
Rural high cost	605.1	2,420.4	39.3
Low income programs	186.1	744.4	12.1
Schools and libraries	526.3	2,105.2	34.1
Rural health care	3.2	12.8	0.2
TOTAL	1,541.7	6,166.8	100%

The schools and libraries program is the second largest segment of the total USF. Yet the Commission's Inspector General has concluded that the program has significant opportunities for fraud.²¹ One way "to ensure the long term stability and sufficiency of the universal service support system" (USF Contrib Mech R&O, ¶ 14) is to ensure that grants under the schools and libraries program are no more than necessary under the 1996 Act.

Another means of limiting the USF contribution factor by limiting the size of the fund itself is to limit the high-cost fund for non-rural carriers by recognizing the size and strengths of those carriers. This subject was extensively discussed in NASUCA's comments (filed December 20, 2002) and reply comments (filed January 17, 2003) on the Joint Board's Recommended Decision on the remand from the Tenth Circuit Court of Appeals in *Qwest Corp. v. FCC*, 258 F.3d 1191 (10th Cir. 2001) ("*Qwest*"). The

²¹ Office of the Inspector General, Semi-Annual Report (October 31, 2002) at 2-10; see also "New York Arrests, FCC Auditor's Warnings Show Prospect for Fraud in USF Programs," *Telecommunications Reports* (January 15, 2003) at 12-13.

Commission's recent actions to make technical modifications to the high-cost model and to refer portability issues to the Joint Board are steps in the right direction.²²

The Federal-State Joint Board on Universal Service is also currently seeking comment on another issue that will have a significant impact on the size of the USF. The issue is the Commission's rules on high-cost universal service support in study areas in which a competitive eligible telecommunications carrier is providing services, and the rules regarding support for second lines, including wireless "lines."²³

On the revenue side, one way to ensure adequate funding for the USF would be to receive appropriate revenues from wireless carriers, currently one of the fastest growing segments of the telecommunications market. In the USF Cont Mech R&O (at ¶ 21), the Commission established a new "safe harbor" for wireless carriers by ruling that these carriers could report 28.5% of their total revenues as interstate without having to produce proof of their actual level of interstate revenues. If such a safe harbor is necessary, the safe harbor may be appropriate for wireless carriers whose revenues are reasonably close to the 28.5% level.²⁴ Use of the safe harbor is totally improper, however, for wireless carriers that receive a substantially greater amount of interstate revenue.

In order to preserve the administrative simplicity of the safe harbor and at the same time capture appropriate revenues from wireless carriers with substantial interstate

²² *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket 96-45, Order (rel. January 7, 2003).

²³ See *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Order, FCC 02-307 (rel. November 8, 2002); *id.*, Public Notice, FCC 03J-1 (rel. February 7, 2003).

²⁴ The need for a wireless safe harbor is based on the notion that wireless carriers cannot accurately identify their interstate traffic. As noted above, some wireless carriers are able to establish a reasonable proxy for their percentage of interstate traffic.

revenues, NASUCA proposes a “three zone” approach. In the first zone, wireless carriers with interstate revenue below 28.5% would be able to use the actual company interstate percentage to calculate their assessment. In the second zone, wireless carriers with interstate revenues between 28.5% and 40% of total revenues could avail themselves of the safe harbor. In the third zone, wireless carriers with interstate revenues greater than 40% of total revenues would have to contribute on the basis of actual interstate revenues.

This three-zone approach thus establishes a “free range” above any safe harbor level for wireless carriers that do not derive a substantial portion of their revenue from the interstate market. On the other hand, wireless carriers with more than 40% of their revenues from the wireless market are substantial providers of interstate telecommunications services and should contribute to the fund on the same non-discriminatory basis as other carriers. As an inducement to compliance, any carrier with actual interstate revenues in excess of 40% of total revenues that failed to report and contribute based on actual revenues should be subject to an enhanced -- substantially increased -- contribution. This and similar enforcement efforts would address the Commission’s concern that bundles have “increased the opportunities to mischaracterize revenues that should be counted for contribution purposes.”²⁵

E. The Commission’s proposed contribution mechanisms improperly base contributions on access to the interstate system, rather than use of the interstate system.

²⁵ USF Contrib Mech R&O, ¶ 3.

Along with the lack of support in the record for the need for the structural change to a connection-based mechanism, there is the fact that a connection-based mechanism violates the law.²⁶ As discussed in the next section, a connection-based mechanism violates 47 U.S.C. § 254(d). As shown here, a connection-based mechanism also violates 47 U.S.C. § 254(k).

The Commission continues to seek comment on the adoption of mechanisms that focus on access to the interstate system, rather than usage. A connection-based mechanism should actually be termed an “access-based mechanism,” because it makes assessments based on consumers’ *capability* to use interstate services and produce interstate revenues for carriers, rather than on the usage of those services. The adoption of a connection-based mechanism because of difficulties with identifying interstate revenues (SFNPRM, ¶ 3) is not justified.

A connection-based universal service connection mechanism that allows or requires pass-through of carrier assessments to consumers would add to the long list of unavoidable surcharges that must be paid by consumers.²⁷ First among these, of course, is the subscriber line charge (“SLC”). Three years ago, in the CALLS Order, the Commission decided that non-traffic sensitive costs that had previously been paid by IXC’s should instead be paid by end users through an increase in a monthly unavoidable

²⁶ As shown below, this includes the “connection-based mechanism with a revenue-based minimum charge” proposed by the Commission in the SFNPRM.

²⁷ All three of the Commission’s proposals apparently presume direct pass-through of the assessments to consumers. See SFNPRM, ¶ 73.

charge, the SLC.²⁸ (“Unavoidable” means that a customer’s failure to pay would result in a disconnection of all telephone service -- local and long distance.)

Yet the USF is also part of the joint and common costs of the telephone network. A carrier’s USF contribution is as much a part of the carrier’s overhead as taxes, franchise fees, and other regulatory costs. Indeed, the Commission’s current USF assessment is the same for all carriers, an equal percentage of revenues. The Commission’s proposed connection-based mechanism would place universal service costs entirely on basic service, in violation of 47 U.S.C. § 254(k):

The Commission, with respect to interstate services ... shall establish any necessary cost allocation rules, accounting safeguards, and guidelines to ensure that services included in the definition of universal service bear no more than a reasonable share of the joint and common costs of facilities used to provide those services.

A connection-based mechanism requires basic service (the services included in the definition of universal service) to bear all of the joint and common cost of universal service support. The costs of universal service should be placed on carriers, not customers, as required by Section 254(d) of the Act. The cost of universal service should be recovered in the price of the services offered by the carriers, not exclusively from basic service in contravention of Section 254(k) of the Act.

²⁸ *Access Charge Reform*, CC Docket Nos. 96-262 and 94-1, *et al.*, Sixth Report and Order, 15 FCC Rcd. 12962 (2000) (“*CALLS Order*”). NASUCA continues to believe that that Commission decision violated the prohibition in 47 U.S.C. § 254(k) against basic service bearing more than a reasonable share of the joint and common costs of the telephone network. See *NASUCA v. FCC*, Sup. Ct. Docket No. 01-968. The Commission felt otherwise (see *CALLS Order*) and two Circuit Courts of Appeal have deferred to the Commission’s judgment. *Texas Office of Public Utility Counsel v. FCC* (“*TOPUC II*”), 265 F.3d 313 (5th Cir. 2001); *Southwestern Bell Telephone Co. v. FCC*, 153 F.3d 523 (8th Cir. 1998).

F. The IXCs that support a connection-based mechanism would be relieved of funding responsibility under the connection-based mechanism.

The 1996 Act directs that

[e]very telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and non-discriminatory basis, to the specific, predictable, and sufficient mechanism established by the Commission to preserve and advance universal service.

47 U.S.C. § 254(d). The current mechanism, based on interstate revenues, assesses carriers based on the amount of money they receive from providing interstate services.

The connection between interstate service and USF assessment is clear. The current revenue-based mechanism is, in concept, both equitable and non-discriminatory, and has been upheld by the courts. See *TOPUC I*, 183 F.3d at 426-430.²⁹

The proposed connection-based mechanisms allow IXCs, which remain the predominant carriers of interstate traffic, to evade almost all responsibility to contribute to universal service, contrary to § 254(d). As the FNPRM stated (at ¶ 36), IXCs “would contribute for multi-line business connections, such as special access, they provide to end users.” In the SFNPRM, the Commission noted the § 254(d) arguments, but expressed no opinion on the merits.³⁰ These arguments will not go away.

Under the connection-based mechanism, the only USF funding responsibility falling on IXCs would be where the IXCs are acting more like local carriers than

²⁹ Notably, after the improvements made on how USF contribution line items for the revenue-based mechanism appear on customers’ bills (USF Contrib Mech R&O, ¶ 45), the SFNPRM no longer claims that a connection-based mechanism will be more understandable for customers as independent support for the connection-based mechanism.

³⁰ SFNPRM, ¶ 71.

interexchange carriers. This is equally true where the IXC's are providing service "as CLECs..." *Id.* This approach ignores the significant level of interstate long distance service otherwise provided by the IXC's.³¹

Under a connection-based proposal, an IXC that was providing only interexchange service, and neither acted as a CLEC nor provided special access to business customers, would be absolved of any responsibility to fund universal service. Even though that IXC is without doubt a telecommunications carrier that provides interstate telecommunications service, under the connection-based mechanism it would avoid paying anything to support federal universal service programs. This would explicitly violate § 254(d), which requires "every telecommunications carrier that provides interstate telecommunications service" to contribute to the USF.

This equation is changed somewhat with the introduction of the minimum bill concept. SFNPRM, ¶ 75. As discussed below, whether a connection-based mechanism with a minimum contribution requirement violates § 254(d) depends on the level of the minimum contribution.

G. Responses to specific requests in the SFNPRM

In the SFNPRM, the Commission first seeks comment on some of the fundamental issues in this proceeding, including whether the changes in the mechanism

³¹ The Commission relied heavily for the connection-based mechanism on an *ex parte* filing of what it called the "USF Coalition." See, e.g., FNPRM footnotes 38, 74, 76, 85, etc. This coalition, referred to in its pleadings as the Coalition for Sustainable Universal Service ("CoSUS") consisted of AT&T, WorldCom, Level 3 Communications and the e-commerce Telecommunications Users Group. USF Contrib Mech R&O, ¶ 4. AT&T and WorldCom will be the principal beneficiaries of the switch to a connections-based mechanism. CoSUS has apparently dissolved. *Id.* CoSUS was as much a misnomer for this group as was the "Coalition for Affordable Local and Long Distance Service."

contained in the USF Contrib Mech R&O are “sufficient to ensure the long-term viability of universal service as the telecommunications market evolves.” SFNPRM, ¶ 67. As discussed above, on the one hand the “problems” with the universal service funding base are much less substantial than posited by the Commission. Equally, the solutions to these “problems” can be accomplished within a revenue-based collection mechanism.

The Commission also seeks comment on a wide variety of issues pertaining to three specific connections-based mechanisms:

1. **“[A] contribution methodology that would impose a minimum contribution obligation on all interstate telecommunications carriers, and a flat charge for each end-user connection....” SFNPRM, ¶ 72.**
2. **“[A]ssess[ing] all connections based purely on capacity....” *Id.***
3. **“[A]ssess[ing] providers of switched connections based on their number of working telephone numbers.” *Id.***

The burden of commenting on these specific proposals lies on those who support these substantial changes to the USF mechanism. NASUCA expects to focus reply comments on the supporters’ arguments for their positions, and on supporters’ estimates of the impact on customers from their proposals.³² There are, however, some of the Commission’s requests for comment that can be responded to now.

³² In a Public Notice released February 26, 2003, the Commission is seeking comment on a staff study that estimates potential assessment levels under the newly modified revenue-based system and three connection-based proposals. It is not clear to what extent this request for comment -- which includes a request for commenters to provide their own estimates, projections, and data -- is intended to supplant the request in the SFNPRM.

1. Connection-based mechanism with minimum contribution for all interstate carriers

The Commission now proposes a revenue-based backstop to the connection-based mechanism. Perhaps this is done as an attempt to address commenters' § 254(d) argument that the connection-based mechanism allows interstate carriers to avoid responsibility for funding the USF. Yet if a revenue-based mechanism is required to augment or correct the flaws in the connection-based mechanism, it is certainly not clear why the connection-based mechanism is needed in the first place.

Having a connection-based mechanism and a revenue-based mechanism operating in tandem will be administratively costly. Carriers will be required to track interstate revenues just as they are currently, but will also have to track connections, however those are defined. Indeed, if one accepts the Commission's fears for the current revenue-based mechanism, the same conditions -- i.e., difficulties of calculating interstate revenues -- would cause the demise of the revenue-based component of a combined mechanism. On the other hand, if one does not accept the gloom-and-doomsaying about the current mechanism, then it is even less obvious why these changes are necessary.

Further, the size of the revenue-based minimum contribution determines whether the combination mechanism satisfies § 254(d). A "de minimis" contribution would be out of step with the law. On the other hand, a system that had a minimal connection-based component but maximized collections based on interstate revenues would be consistent with the statute. The Commission will be hard-pressed to justify any point in between that represents a combination connection-based mechanism and a minimum bill.

For example, the Commission has given an example of a minimum 1% assessment for carriers that have no connections. SFNPRM, ¶ 78. Although this might

appear reasonable for a low-revenue carrier -- which would contribute \$1,000 on \$100,000 annual interstate revenue -- if the carrier instead had \$100,000,000 in interstate revenues -- but provided no direct connections -- the carrier would contribute 1% (or \$1,000,000) compared to the \$8.7 million contributed under an 8.7% contribution factor in the current revenue-based system.

2. Assessing all connections based purely on capacity, splitting contributions between switched transport and access

It must first be noted that, despite the Commission's description of this proposal as based "purely" on capacity (*id.* at ¶ 71), the proposal set forth in the SFNPRM would in fact "assess interstate telecommunications services not directly tied to connections based on revenues." *Id.* at ¶ 86. Most of the questions about a combination mechanism raised above thus apply here as well.

The Commission also discusses a key aspect of the connection-based mechanisms: the use of capacity tiers for determining the assessment rate. *Id.*, ¶ 87; see also *id.*, ¶ 80-83. The single-function percentage assessment on revenues under the current mechanism allows the same rate to be applied to interstate revenues of \$100,000 and to \$1,000,000,000. The stair-step function of the Commission's connection-based proposals, however, will be a source of confusion and attempts to evade a higher level of assessment.

3. Phone numbers

This late entrant into the connection-based race raises a unique set of issues (see *id.*, ¶¶ 97-98), without really adding any special superiority to the mix. NASUCA hopes

that the comments of the supporters of the number-based mechanism will fill in some of these blanks.

The SFNPRM mentions that using working numbers as the assessment base for the USF might produce an ancillary benefit of number conservation. *Id.*, ¶ 96. The AT&T and Ad Hoc proposals assess providers based on telephone numbers assigned to end users (*id.*). Thus the use of this mechanism will conserve numbers only if carriers are now assigning numbers to end users when there is actually no end user. If the USF contribution methodology is to be used as a number conservation tool, the proper focus for number conservation would be on numbers that carriers reserve, rather than on numbers actually assigned to customers.

Further, a numbers-based contribution mechanism will aid in number conservation only if carriers are forbidden from establishing surcharges that guarantee recovery of the contribution. When carriers can pass through the contribution to their customers on a line-item basis, they have no incentive to limit the level of the contribution.

H. Conclusion

Assurance of continued sufficient USF funding (FNPRM, ¶ 15) has little to do with the structure of the collection mechanism. The three Commission proposals do not ensure adequate funding; on the other hand, the current structure does not necessarily make adequate funding more difficult.

There is no need for the adoption of a connection-based USF contribution mechanism at this time. The current mechanism should be improved to ensure that all

interstate services that are not *de minimis* are assessed to support universal service on an equitable and non-discriminatory basis.

If in the future the burden on customers from the current mechanism becomes unreasonable, either from a decrease in the interstate revenue base or from increased needs of the fund, the Commission may consider switching to a different mechanism. Before doing so, the Commission must have clear information about the impact of the change on different industry and customer segments. See SFPRM, ¶ 73. This should also include the same information about the current mechanism (*id.*) that was absent from the comments previously submitted.³³ That different mechanism -- whether or not connection-based, such as currently proposed by the Commission -- 1) should ensure that the broadest possible contribution base is used; 2) should not allow any sector of the industry to avoid appropriate contribution responsibility; 3) should not unduly burden any segment of any class of customer; and 4) should be capped, for residential wireline customers at least, for five years in order to achieve funding stability.

Respectfully submitted,

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³³ See NASUCA Comments (April 22, 2002) at 12-13.

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